

FIRST CITIZENS BANCSHARES INC /DE/

Form 10-Q

August 02, 2018

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2018

or

.. Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 001-16715

First Citizens BancShares, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	56-1528994
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

4300 Six Forks Road, Raleigh, North Carolina	27609
(Address of principle executive offices)	(Zip code)
(919) 716-7000	
(Registrant's telephone number, including area code)	

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days. Yes x No ..

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the Registrant was required to submit and post such files) Yes x No ..

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "larger accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer	x	Accelerated filer	..
Non-accelerated filer	..	Smaller reporting company	..
		Emerging growth company	..

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ..

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes .. No x

Class A Common Stock—\$1 Par Value—11,005,220 shares

Class B Common Stock—\$1 Par Value—1,005,185 shares

(Number of shares outstanding, by class, as of August 1, 2018)

Table of Contents

INDEX

Page No.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets (Unaudited) 3

Consolidated Statements of Income (Unaudited) 4

Consolidated Statements of Comprehensive Income (Unaudited) 5

Consolidated Statements of Changes in Shareholders' Equity (Unaudited) 6

Consolidated Statements of Cash Flows (Unaudited) 7

Notes to Consolidated Financial Statements (Unaudited) 8

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 40

Item 3. Quantitative and Qualitative Disclosures about Market Risk 63

Item 4. Controls and Procedures 63

PART II. OTHER INFORMATION

Item 1. Legal Proceedings 64

Item 1A. Risk Factors 64

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds 64

Item 6. Exhibits 64

Table of Contents

PART I

Item 1. Financial Statements

First Citizens BancShares, Inc. and Subsidiaries
Consolidated Balance Sheets

(Dollars in thousands, unaudited)	June 30, 2018	December 31, 2017
Assets		
Cash and due from banks	\$260,525	\$336,150
Overnight investments	1,223,311	1,387,927
Investment in marketable equity securities	107,264	—
Investment securities available for sale	4,783,507	7,180,180
Investment securities held to maturity	2,299,774	76
Loans held for sale	58,961	51,179
Loans and leases	24,538,437	23,596,825
Allowance for loan and lease losses	(224,865)	(221,893)
Net loans and leases	24,313,572	23,374,932
Premises and equipment	1,167,532	1,138,431
Other real estate owned	46,633	51,097
Income earned not collected	99,567	95,249
Goodwill	208,217	150,601
Other intangible assets	77,370	73,096
Other assets	442,333	688,594
Total assets	\$35,088,566	\$34,527,512
Liabilities		
Deposits:		
Noninterest-bearing	\$12,181,717	\$11,237,375
Interest-bearing	18,227,167	18,028,900
Total deposits	30,408,884	29,266,275
Short-term borrowings	613,993	693,807
Long-term obligations	241,360	870,240
FDIC shared-loss payable	103,487	101,342
Other liabilities	273,956	261,784
Total liabilities	31,641,680	31,193,448
Shareholders' equity		
Common stock:		
Class A - \$1 par value (16,000,000 shares authorized; 11,005,220 shares issued and outstanding at June 30, 2018 and December 31, 2017)	11,005	11,005
Class B - \$1 par value (2,000,000 shares authorized; 1,005,185 shares issued and outstanding at June 30, 2018 and December 31, 2017)	1,005	1,005
Preferred stock - \$0.01 par value (10,000,000 shares authorized; no shares issued and outstanding at June 30, 2018 and December 31, 2017)	—	—
Surplus	658,918	658,918
Retained earnings	3,020,596	2,785,430
Accumulated other comprehensive loss	(244,638)	(122,294)
Total shareholders' equity	3,446,886	3,334,064

Total liabilities and shareholders' equity	\$35,088,566	\$34,527,512
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See accompanying Notes to Consolidated Financial Statements.

3

Table of ContentsFirst Citizens BancShares, Inc. and Subsidiaries
Consolidated Statements of Income

	Three months ended June 30		Six months ended June 30	
(Dollars in thousands, except per share data, unaudited)	2018	2017	2018	2017
Interest income				
Loans and leases	\$261,086	\$235,732	\$513,068	\$462,362
Investment securities and dividend income	37,179	30,406	72,199	60,157
Overnight investments	5,612	6,404	11,211	10,880
Total interest income	303,877	272,542	596,478	533,399
Interest expense				
Deposits	4,521	4,132	8,277	8,568
Short-term borrowings	821	1,176	2,255	1,756
Long-term obligations	2,316	5,625	5,290	11,123
Total interest expense	7,658	10,933	15,822	21,447
Net interest income	296,219	261,609	580,656	511,952
Provision for loan and lease losses	8,438	12,324	16,043	20,555
Net interest income after provision for loan and lease losses	287,781	249,285	564,613	491,397
Noninterest income				
Gain on acquisitions	—	122,728	—	134,745
Cardholder services, net	14,925	14,518	29,707	27,361
Merchant services, net	6,478	5,800	12,655	11,556
Service charges on deposit accounts	25,952	25,862	52,495	48,004
Wealth management services	25,515	21,920	49,084	42,882
Securities gains, net	—	3,351	—	3,327
Marketable equity securities gains, net	4,440	—	5,411	—
Other service charges and fees	7,756	6,628	15,236	14,229
Mortgage income	4,703	4,966	8,940	12,542
Insurance commissions	2,940	2,563	6,716	6,121
ATM income	2,217	2,513	4,388	4,286
Net impact from FDIC shared-loss agreement termination	—	—	—	(45)
Gain on extinguishment of debt	—	—	25,814	—
Other	6,001	6,792	13,165	12,279
Total noninterest income	100,927	217,641	223,611	317,287
Noninterest expense				
Salaries and wages	129,841	121,826	259,044	238,188
Employee benefits	29,715	25,383	61,806	52,560
Occupancy expense	26,100	26,059	54,054	50,821
Equipment expense	25,167	24,654	50,141	49,242
FDIC insurance expense	5,492	5,705	11,225	11,298
Collection and foreclosure-related expenses	3,974	2,376	8,120	6,139
Merger-related expenses	2,412	6,853	3,010	7,686
Other	43,292	42,191	86,656	75,812
Total noninterest expense	265,993	255,047	534,056	491,746
Income before income taxes	122,715	211,879	254,168	316,938
Income taxes	29,424	77,219	60,646	114,657
Net income	\$93,291	\$134,660	\$193,522	\$202,281
Average shares outstanding	12,010,405	12,010,405	12,010,405	12,010,405

Net income per share	\$7.77	\$ 11.21	\$16.11	\$16.84
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See accompanying Notes to Consolidated Financial Statements.

Table of ContentsFirst Citizens BancShares, Inc. and Subsidiaries
Consolidated Statements of Comprehensive Income

	Three months ended June 30		Six months ended June 30	
(Dollars in thousands, unaudited)	2018	2017	2018	2017
Net income	\$93,291	\$134,660	\$193,522	\$202,281
Other comprehensive (loss) income:				
Unrealized gains on securities available for sale:				
Change in unrealized securities available for sale gains arising during period	82,789	13,771	4,155	49,867
Tax effect	(19,042)	(5,125)	(954)	(18,544)
Reclassification adjustment for gains included in income before income taxes	—	(3,351)	—	(3,327)
Tax effect	—	1,240	—	1,231
Total change in unrealized gains on securities available for sale, net of tax	63,747	6,535	3,201	29,227
Unrealized losses on securities available for sale transferred to held to maturity:				
Unrealized losses on securities available for sale transferred to held to maturity	(109,507)	—	(109,507)	—
Tax effect	25,186	—	25,186	—
Reclassification adjustment for accretion of unrealized losses on securities available for sale transferred to held to maturity	4,473	—	4,473	—
Tax effect	(1,028)	—	(1,028)	—
Total change in unrealized losses on securities available for sale transferred to held to maturity, net of tax	(80,876)	—	(80,876)	—
Change in pension obligation:				
Amortization of actuarial losses and prior service cost	3,654	2,460	6,991	4,960
Tax effect	(840)	(897)	(1,608)	(1,838)
Total change in pension obligation, net of tax	2,814	1,563	5,383	3,122
Other comprehensive (loss) income	(14,315)	8,098	(72,292)	32,349
Total comprehensive income	\$78,976	\$142,758	\$121,230	\$234,630

See accompanying Notes to Consolidated Financial Statements.

Table of ContentsFirst Citizens BancShares, Inc. and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity

(Dollars in thousands, unaudited)	Class A Common Stock	Class B Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
Balance at December 31, 2016	\$ 11,005	\$ 1,005	\$658,918	\$2,476,691	\$ (135,192)	\$3,012,427
Net income	—	—	—	202,281	—	202,281
Other comprehensive income, net of tax	—	—	—	—	32,349	32,349
Cash dividends (\$0.60 per share)	—	—	—	(7,206)	—	(7,206)
Balance at June 30, 2017	\$ 11,005	\$ 1,005	\$658,918	\$2,671,766	\$ (102,843)	\$3,239,851
Balance at December 31, 2017	\$ 11,005	\$ 1,005	\$658,918	\$2,785,430	\$ (122,294)	\$3,334,064
Cumulative effect of adoption of ASU 2016-01	—	—	—	18,716	(18,716)	—
Cumulative effect of adoption of ASU 2018-02	—	—	—	31,336	(31,336)	—
Net income	—	—	—	193,522	—	193,522
Other comprehensive loss, net of tax	—	—	—	—	(72,292)	(72,292)
Cash dividends (\$0.70 per share)	—	—	—	(8,408)	—	(8,408)
Balance at June 30, 2018	\$ 11,005	\$ 1,005	\$658,918	\$3,020,596	\$ (244,638)	\$3,446,886

See accompanying Notes to Consolidated Financial Statements.

Table of ContentsFirst Citizens BancShares, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

	Six months ended June 30	
	2018	2017
(Dollars in thousands, unaudited)		
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 193,522	\$ 202,281
Adjustments to reconcile net income to cash provided by operating activities:		
Provision for loan and lease losses	16,043	20,555
Deferred tax (benefit) expense	(2,835)	45,628
Net change in current taxes	(16,609)	17,404
Depreciation	47,343	45,420
Net (decrease) increase in accrued interest payable	(2,043)	1,344
Net increase in income earned not collected	(1,601)	(290)
Gain on acquisitions	—	(134,745)
Securities gains, net	—	(3,327)
Marketable equity securities gains, net	(5,411)	—
Gain on extinguishment of debt	(25,814)	—
Loss on termination of FDIC shared-loss agreements	—	45
Origination of loans held for sale	(304,580)	(299,136)
Proceeds from sale of loans held for sale	302,766	309,791
Gain on sale of loans held for sale	(5,610)	(6,279)
Gain on sale of portfolio loans	—	(164)
Net write-downs/losses on other real estate	2,698	2,160
Gain on sales of premises and equipment	—	(159)
Net accretion of premiums and discounts	(17,240)	(22,918)
Amortization of intangible assets	11,562	11,045
Net change in FDIC receivable for shared-loss agreements	—	4,821
Net change in FDIC payable for shared-loss agreements	2,145	2,118
Net change in other assets	310,635	(34,340)
Net change in other liabilities	14,998	29,647
Net cash provided by operating activities	519,969	190,901
CASH FLOWS FROM INVESTING ACTIVITIES		
Net increase in loans outstanding	(360,764)	(462,385)
Purchases of investment securities available for sale	(920,356)	(1,186,883)
Purchases of marketable equity securities	(2,818)	—
Proceeds from maturities/calls of investment securities held to maturity	78,384	18
Proceeds from maturities/calls of investment securities available for sale	797,739	1,140,459
Proceeds from sales of investment securities available for sale	119,273	517,588
Proceeds from sales of marketable equity securities	8,493	—
Net decrease (increase) in overnight investments	175,009	(908,583)
Proceeds from sales of portfolio loans	—	32,294
Cash paid to the FDIC for shared-loss agreements	—	(5,197)
Net cash paid to the FDIC for termination of shared-loss agreements	—	(285)
Proceeds from sales of other real estate	15,769	20,236
Proceeds from sales of premises and equipment	198	2,305
Purchases of premises and equipment	(59,603)	(35,912)
Business acquisitions, net of cash acquired	(106,298)	300,703
Net cash used in investing activities	(254,974)	(585,642)

CASH FLOWS FROM FINANCING ACTIVITIES

Net decrease in time deposits	(181,889)	(238,751)
Net increase in demand and other interest-bearing deposits	704,909	429,684
Net (decrease) increase in short-term borrowings	(201,303)	61,030
Repayment of long-term obligations	(653,929)	(7,985)
Origination of long-term obligations	—	175,000
Cash dividends paid	(8,408)	(7,206)
Net cash (used in) provided by financing activities	(340,620)	411,772
Change in cash and due from banks	(75,625)	17,031
Cash and due from banks at beginning of period	336,150	539,741
Cash and due from banks at end of period	\$260,525	\$556,772

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:

Transfers of loans to other real estate	\$11,868	\$21,891
Dividends declared but not paid	4,204	3,603
Reclassification of portfolio loans to loans held for sale	—	84,509
Transfer of investment securities available for sale to held to maturity	2,486,761	—

See accompanying Notes to Consolidated Financial Statements.

Table of Contents

First Citizens BancShares, Inc. and Subsidiaries
Notes to Unaudited Consolidated Financial Statements

NOTE A - ACCOUNTING POLICIES AND BASIS OF PRESENTATION

First Citizens BancShares, Inc. (BancShares) is a financial holding company organized under the laws of Delaware and conducts operations through its banking subsidiary, First-Citizens Bank & Trust Company (FCB), which is headquartered in Raleigh, North Carolina.

General

These consolidated financial statements and notes thereto are presented in accordance with instructions for Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all information and notes necessary for a complete presentation of financial position, results of operations and cash flow activity required in accordance with accounting principles generally accepted in the United States of America (GAAP). In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the consolidated financial position and consolidated results of operations have been made. The unaudited interim consolidated financial statements included in this Form 10-Q should be read in conjunction with the consolidated financial statements and notes to consolidated financial statements included in BancShares' Annual Report on Form 10-K for the year ended December 31, 2017.

Reclassifications

In certain instances, amounts reported in prior years' consolidated financial statements have been reclassified to conform to the current financial statement presentation. Such reclassifications had no effect on previously reported cash flows, shareholders' equity or net income.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported. Actual results could differ from those estimates, and different assumptions in the application of these policies could result in material changes in BancShares' consolidated financial position, the consolidated results of its operations or related disclosures. Material estimates that are particularly susceptible to significant change include:

- Allowance for loan and lease losses;
- Fair value of financial instruments, including acquired assets and assumed liabilities;
- Pension plan assumptions;
- Cash flow estimates on purchased credit-impaired (PCI) loans;
- Goodwill and other intangible assets;
- Federal Deposit Insurance Corporation (FDIC) shared-loss payable; and
- Income tax assets, liabilities and expense

Recently Adopted Accounting Pronouncements

FASB ASU 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

This ASU requires a reclassification from accumulated other comprehensive income (AOCI) to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate in the Tax Cuts and Jobs Act of 2017 (Tax Act), which was enacted on December 22, 2017. The Tax Act included a reduction to the corporate income tax rate from 35 percent to 21 percent effective January 1, 2018. The amount of the reclassification would be the difference between the historical corporate income tax rate and the newly enacted 21 percent corporate income tax rate.

The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. We adopted the guidance effective in the first quarter of 2018. The change in accounting principle was accounted for as a cumulative-effect adjustment to the balance sheet

resulting in a \$31.3 million increase to retained earnings and a corresponding decrease to AOCI on January 1, 2018.

Table of Contents

FASB ASU 2017-07, Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

This ASU requires employers to present the service cost component of the net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. Employers will present the other components separately from the line item that includes the service cost. In addition, only the service cost component of net benefit cost is eligible for capitalization.

The amendments in this ASU are effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We adopted the guidance effective in the first quarter of 2018. The adoption did not have a material impact on our consolidated financial position or consolidated results of operations.

FASB ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities

This ASU addresses certain aspects of recognition, measurement, presentation and disclosure of certain financial instruments. The amendments in this ASU (1) require most equity investments to be measured at fair value with changes in fair value recognized in net income; (2) simplify the impairment assessment of equity investments without a readily determinable fair value; (3) eliminate the requirement to disclose the method(s) and significant assumptions used to estimate the fair value for financial instruments measured at amortized cost on the balance sheet; (4) require public business entities to use exit price notion, rather than entry prices, when measuring fair value of financial instruments for disclosure purposes; (5) require separate presentation of financial assets and financial liabilities by measurement category and form of financial assets on the balance sheet or the accompanying notes to the financial statements; (6) require separate presentation in other comprehensive income of the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the organization has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; and (7) state that a valuation allowance on deferred tax assets related to available-for-sale securities should be evaluated in combination with other deferred tax assets.

The amendments in this ASU are effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We adopted the guidance effective in the first quarter of 2018. The change in accounting principle was accounted for as a cumulative-effect adjustment to the balance sheet resulting in an \$18.7 million increase to retained earnings and a decrease to AOCI on January 1, 2018. With the adoption of this ASU equity securities can no longer be classified as available for sale, as such marketable equity securities are disclosed as a separate line item on the balance sheet with changes in the fair value of equity securities reflected in net income.

For equity investments without a readily determinable fair value, BancShares has elected to measure the equity investments using the measurement alternative which requires BancShares to make a qualitative assessment of whether the investment is impaired at each reporting period. Under the measurement alternative these investments will be measured at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer. If a qualitative assessment indicates that the investment is impaired, BancShares will estimate the investment's fair value in accordance with ASC 820 and, if the fair value is less than the investment's carrying value, recognize an impairment loss in net income equal to the difference between carrying value and fair value. Equity investments without a readily determinable fair value are recorded within other assets in the consolidated balance sheets.

FASB ASU 2014-09, Revenue from Contracts with Customers (Topic 606)

In May 2014, the FASB issued a standard on the recognition of revenue from contracts with customers with the core principle being for a company to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard, which provides a five step model to determine when and how revenue is recognized, also results in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively and improves guidance for multiple-element arrangements.

Per ASU 2015-14, Deferral of the Effective Date, this guidance was deferred and is effective for fiscal periods beginning after December 15, 2017, including interim reporting periods within that reporting period. We adopted the guidance effective in the first quarter of 2018. Our revenue is comprised primarily of net interest income on financial assets and liabilities, which is explicitly excluded from the scope of the new guidance, and noninterest income. The contracts that are in scope of the guidance are primarily related to cardholder and merchant services income, service charges on deposit accounts, wealth management services income, other service charges and fees, insurance commissions, ATM income, sales of other real estate and other. Based on our overall assessment of revenue streams and review of related contracts affected by the ASU, the adoption of this guidance did not change the method in which we currently recognize revenue.

Table of Contents

We also completed an evaluation of the costs related to these revenue streams to determine whether such costs should be presented as expenses or contra-revenue (i.e., gross vs. net). Based on this evaluation, we determined that the classification of cardholder and merchant processing costs as well as expenses for cardholder reward programs should be netted against cardholder and merchant services income. We used the full retrospective method of adoption and restated the prior financial statements to net the cardholder and merchant processing costs against the related cardholder and merchant services income. These classification changes resulted in changes to both noninterest income and noninterest expense, however, there was no change to previously reported net income. Merchant processing expenses of \$20.8 million and \$40.0 million have been reclassified and reported as a component of merchant services income for the three and six months ended June 30, 2017, respectively. Cardholder processing expenses of \$6.8 million and cardholder reward programs expense of \$3.0 million have been reclassified and reported as a component of cardholder services income for the three months ended June 30, 2017. For the six months ended June 30, 2017, cardholder processing expenses of \$12.7 million and cardholder reward programs expense of \$5.5 million were reclassified and reported as a component of cardholder services income.

Revenue Recognition

The standard requires disclosure of qualitative and quantitative information surrounding the amount, nature, timing and uncertainty of revenues and cash flows arising from contracts with customers. The core principle of the new standard is that revenue should be recognized when a company transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services.

Descriptions of our noninterest revenue-generating activities that are within the scope of the new revenue ASU is broadly segregated as follows:

Cardholder and Merchant Services - These represent interchange fees from customer debit and credit card transactions that are earned at the time a cardholder engages in a transaction with a merchant as well as fees charged to merchants for providing them the ability to accept and process the debit and credit card transaction. Revenue is recognized when the performance obligation has been met as it is satisfied upon the completion of the card transaction. Additionally, ASU 2014-09 requires costs associated with cardholder and merchant services transactions to be netted against the fees from such transactions when an entity is acting as an agent in providing services to a customer.

Service Charges on Deposit Accounts - These deposit account-related fees represent monthly account maintenance and transaction-based service fees such as overdraft fees, stop payment fees and charges for issuing cashier's checks and money orders. For account maintenance services, revenue is recognized at the end of the statement period when our performance obligation has been satisfied. All other revenues from transaction-based services are recognized at a point in time when the performance obligation has been completed.

Wealth Management Services - These primarily represent annuity fees, sales commissions, management fees, insurance sales, and trust and asset management fees. The performance obligation for wealth management services is the provision of services to place annuity products issued by the counterparty to investors, and the provision of services to manage the client's assets, including brokerage custodial and other management services. Revenue is recognized over the period in which services are performed, are based on a percentage of the value of the assets under management/administration, and are fixed or variable based on account type, or are transaction-based.

Other Service Charges and Fees - These include, but are not limited to, check cashing fees, international banking fees, internet banking fees, wire transfer fees and safe deposit fees. These fees are charged, and revenue is recognized, at the point in time the service being requested by the customer is provided thus satisfying our performance obligation.

Insurance Commissions - These represent commissions earned on the issuance of insurance products and services. The performance obligation is generally satisfied upon the issuance of the insurance policy and revenue is recognized when the commission payment is remitted by the insurance carrier or policy holder depending on if the billing is performed by FCB or the carrier.

ATM Income - These represent fees imposed on customers and non-customers for engaging in an ATM transaction. Revenue is recognized at the time of the transaction as the performance obligation of rendering the ATM service has been met.

Sales of Other Real Estate - ORE property consists of foreclosed real estate used as collateral for loans, closed branches, land acquired and no longer intended for future use by FCB, and other real estate purchased for resale as ORE. Revenue is generally recognized on the date of sale where the performance obligation of providing access and transferring control of the specified ORE property to the buyer in good faith and good title is satisfied. This is recorded as a component of other noninterest income.

Other - This consists of several forms of recurring revenue such as external rental income, parking income, FHLB dividends, and income earned on changes in the cash surrender value of bank-owned life insurance, all of which are outside the scope of ASU

Table of Contents

2014-09. The remaining miscellaneous income is the result of immaterial transactions where revenue is recognized when, or as, the performance obligation is satisfied.

Recently Issued Accounting Pronouncements

FASB ASU 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment
This ASU eliminates Step 2 from the goodwill impairment test. Under Step 2, an entity had to perform procedures to determine the fair value at the impairment testing date of its assets and liabilities (including unrecognized assets and liabilities) following the procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Instead, under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, an entity should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. This ASU eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative test.

This ASU will be effective for BancShares' annual or interim goodwill impairment tests for fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. We expect to adopt the guidance for our annual impairment test in fiscal year 2020. BancShares does not anticipate any impact to our consolidated financial position or consolidated results of operations as a result of the adoption.

FASB ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments

This ASU eliminates the delayed recognition of the full amount of credit losses until the loss was probable of occurring and instead will reflect an entity's current estimate of all expected credit losses. The amendments in this ASU broaden the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The ASU does not specify a method for measuring expected credit losses and allows an entity to apply methods that reasonably reflect its expectations of the credit loss estimate based on the entity's size, complexity and risk profile. In addition, the disclosures of credit quality indicators in relation to the amortized cost of financing receivables, a current disclosure requirement, are further disaggregated by year of origination.

The amendments in this ASU are effective for public business entities for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for fiscal years beginning after December 15, 2018. We will adopt the guidance by the first quarter of 2020 with a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption. For BancShares, the standard will apply to loans, unfunded loan commitments and debt securities. A cross-functional team co-led by Corporate Finance and Risk Management is in place to implement the new standard. The team continues to work on critical activities such as building models, documenting accounting policies, reviewing data quality, and implementing a reporting and disclosure solution. We continue to evaluate the impact the new standard will have on our consolidated financial statements but the magnitude of this impact has not been determined. The final impact will be dependent, among other items, on loan portfolio composition and credit quality at the adoption date, as well as economic conditions, financial models used and forecasts at that time.

FASB ASU 2016-02, Leases (Topic 842)

This ASU increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The key difference between existing standards and this ASU is the requirement for lessees to recognize all lease contracts on their balance sheet. This ASU requires lessees to classify leases as either operating or finance leases, which are substantially similar to the current operating and capital leases classifications. The distinction between these two classifications under the new standard does not relate to balance sheet treatment, but relates to treatment in the statements of income and cash

flows. Lessor guidance remains largely unchanged with the exception of how a lessor determines the appropriate lease classification for each lease to better align the lessor guidance with revised lessee classification guidance.

The amendments in this ASU are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. We will adopt during the first quarter of 2019. We expect an increase to the Consolidated Balance Sheets for right-of-use assets and associated lease liabilities, as well as resulting depreciation expense of the right-of-use assets and interest expense of the lease liabilities in the Consolidated Statements of Income, for arrangements previously accounted for as operating leases. Additionally, adding these assets to our balance sheet will impact our

Table of Contents

total risk-weighted assets used to determine our regulatory capital levels. Our impact analysis on this change in accounting principle estimates an increase to the Consolidated Balance Sheets for total lease liability ranging between \$65.0 million and \$85.0 million, as the initial gross up of both assets and liabilities. Capital is expected to be adversely impacted by an estimated four to six basis points. These are preliminary estimates subject to change and will continue to be refined closer to adoption.

NOTE B - BUSINESS COMBINATIONS

Palmetto Heritage Bancshares, Inc.

On July 25, 2018, First Citizens Bank and Palmetto Heritage Bancshares, Inc. announced the signing of a definitive merger agreement. The agreement provides for the acquisition of Pawley's Island, SC-based Palmetto Heritage Bancshares. Under the terms of the agreement, cash consideration of \$135.00 per share will be paid to the shareholders of Palmetto Heritage Bancshares for each share of Palmetto Heritage's common stock with total consideration paid of \$30.3 million. The transaction is expected to close during the fourth quarter of 2018, subject to the receipt of regulatory approvals and the approval of Palmetto Heritage Bancshares' shareholders. As of June 30, 2018, Palmetto Heritage Bancshares reported \$167.9 million in consolidated assets, \$137.8 million in loans and \$126.4 million in deposits.

Capital Commerce Bancorp, Inc.

On June 27, 2018, FCB and Capital Commerce Bancorp, Inc. (Capital Commerce) entered into a definitive merger agreement. The agreement provides for the acquisition of Milwaukee, Wisconsin-based Capital Commerce by FCB. Under the terms of the agreement, cash consideration of \$4.75 per share will be paid to the shareholders of Capital Commerce for each share of Capital Commerce's common stock totaling approximately \$28.1 million. The transaction is expected to close no later than the fourth quarter of 2018, subject to the receipt of regulatory approvals and the approval of Capital Commerce's shareholders, and will be accounted for under the acquisition method of accounting. The merger will allow FCB to expand its presence and enhance banking efforts in the Milwaukee market. As of March 31, 2018, Capital Commerce reported \$216.2 million in consolidated assets, \$180.6 million in loans and \$171.0 million in deposits.

HomeBancorp, Inc.

On May 1, 2018, FCB completed the merger of Tampa, Florida-based HomeBancorp, Inc. (HomeBancorp) and its subsidiary, HomeBanc, into FCB. Under the terms of the merger agreement, cash consideration of \$15.03 was paid to the shareholders of HomeBancorp for each share of HomeBancorp's common stock and total consideration was \$112.7 million. The merger allowed FCB to expand its footprint in Florida by entering into two new markets in Tampa and Orlando.

The HomeBancorp transaction was accounted for under the acquisition method of accounting and, accordingly, assets acquired and liabilities assumed were recorded at their estimated fair values on the acquisition date. Fair values are preliminary and subject to refinement for up to one year after the closing date of the acquisition as additional information regarding closing date fair values becomes available.

The fair value of the assets acquired was \$842.7 million, including \$550.6 million in non-purchased credit impaired (non-PCI) loans, \$15.6 million in purchased credit impaired (PCI) loans and \$9.9 million in a core deposit intangible. Liabilities assumed were \$787.7 million, of which \$619.6 million were deposits. As a result of the transaction, FCB recorded \$57.6 million of goodwill. The amount of goodwill represents the excess purchase price over the estimated fair value of the net assets acquired. The premium paid reflects the increased market share and related synergies that are expected to result from the acquisition. None of the goodwill is deductible for income tax purposes as the merger is accounted for as a qualified stock purchase.

Based on such credit factors as past due status, nonaccrual status, loan-to-value, credit scores, and other quantitative and qualitative considerations, the acquired loans were separated into loans with evidence of credit deterioration, which are accounted for under ASC 310-30 (PCI loans), and loans that do not meet this criteria, which are accounted for under ASC 310-20 (non-PCI loans).

Table of Contents

The following table provides the purchase price as of the acquisition date and the identifiable assets acquired and liabilities assumed at their estimated fair values.

(Dollars in thousands)	As recorded by FCB	
Purchase Price		\$112,657
Assets		
Cash and due from banks	\$6,359	
Overnight investments	10,393	
Investment securities	200,918	
Loans held for sale	791	
Loans	566,173	
Premises and equipment	6,542	
Other real estate owned	2,135	
Income earned not collected	2,717	
Intangible assets	13,206	
Other assets	33,459	
Total assets acquired	842,693	
Liabilities		
Deposits	619,589	
Short-term borrowings	108,973	
Accrued interest payable	1,020	
Long-term obligations	52,944	
Other liabilities	5,126	
Total liabilities assumed	\$787,652	
Fair value of net assets assumed		55,041
Goodwill recorded for HomeBancorp		\$57,616

Merger-related expenses of \$1.5 million and \$1.7 million were recorded in the Consolidated Statements of Income for the three and six months ended June 30, 2018. Loan-related interest income generated from HomeBancorp was approximately \$5.0 million since the acquisition date. The ongoing contributions of this transaction to BancShares' financial statements is not considered material, and therefore pro forma financial data is not included.

Table of Contents

NOTE C - INVESTMENTS

The amortized cost and fair value of investment securities classified as available for sale and held to maturity at June 30, 2018 and December 31, 2017, were as follows:

June 30, 2018				
(Dollars in thousands)	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Investment securities available for sale				
U.S. Treasury	\$1,508,435	\$ —	\$ 4,461	\$1,503,974
Government agency	131,233	157	355	131,035
Mortgage-backed securities	3,104,316	1,621	71,872	3,034,065
Corporate bonds	108,649	391	250	108,790
Other	5,545	98	—	5,643
Total investment securities available for sale	\$4,858,178	\$ 2,267	\$ 76,938	\$4,783,507

December 31, 2017				
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Investment securities available for sale				
U.S. Treasury	\$1,658,410	\$ —	\$ 546	\$1,657,864
Government agency	8,695	15	40	8,670
Mortgage-backed securities	5,419,379	1,529	80,152	5,340,756
Equity securities	75,471	29,737	—	105,208
Corporate bonds	59,414	557	8	59,963
Other	7,645	256	182	7,719
Total investment securities available for sale	\$7,229,014	\$ 32,094	\$ 80,928	\$7,180,180

June 30, 2018				
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Investment securities held to maturity				
Mortgage-backed securities	\$2,299,774	\$ 3,778	\$ 1,459	\$2,302,093

December 31, 2017				
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Investment securities held to maturity				
Mortgage-backed securities	\$76	\$ 5	\$ —	\$81

As a result of adopting ASU 2016-01 in the first quarter of 2018, investments in marketable equity securities are no longer classified as investments available for sale. At June 30, 2018 and December 31, 2017, we had \$107.3 million and \$105.2 million, respectively, in marketable equity securities recorded at fair value. Prior to January 1, 2018 equity securities were classified as available for sale and stated at fair value with unrealized gains and losses reported in accumulated other comprehensive income. A cumulative-effect adjustment of \$18.7 million was recorded on January 1, 2018 to reclassify the net unrealized gains from accumulated other comprehensive income to retained earnings with subsequent changes in fair value recognized in the Consolidated Statements of Income.

On May 1, 2018, mortgage-backed securities with an amortized cost of \$2.49 billion were transferred from investments available for sale to the held to maturity portfolio. At the time of transfer, the mortgage-backed securities had a fair value of \$2.38 billion and a weighted average contractual maturity of 13 years. The unrealized loss on these securities at the date of transfer was \$109.5 million and continues to be reported as a component of AOCI. This unrealized loss will be accreted over the remaining expected life of the securities as an adjustment of yield and is offset by the amortization of the corresponding discount on the transferred securities. FCB has the intent and ability to retain these securities until maturity.

Investments in mortgage-backed securities primarily represent securities issued by the Government National Mortgage Association, Federal National Mortgage Association and Federal Home Loan Mortgage Corporation. Investments in government agency securities represent securities issued by the United States Small Business Administration. Investments in corporate bonds and

Table of Contents

marketable equity securities represent positions in securities of other financial institutions. Other investments include trust preferred securities of financial institutions. The following table provides the amortized cost and fair value by contractual maturity. Expected maturities will differ from contractual maturities on certain securities because borrowers and issuers may have the right to call or prepay obligations with or without prepayment penalties. Repayments of mortgage-backed securities are dependent on the repayments of the underlying loan balances.

	June 30, 2018		December 31, 2017	
(Dollars in thousands)	Cost	Fair value	Cost	Fair value
Investment securities available for sale				
Non-amortizing securities maturing in:				
One year or less	\$1,255,746	\$1,252,487	\$808,768	\$808,301
One through five years	252,689	251,487	849,642	849,563
Five through 10 years	108,649	108,790	59,414	59,963
Over 10 years	5,545	5,643	7,645	7,719
Government agency	131,233	131,035	8,695	8,670
Mortgage-backed securities	3,104,316	3,034,065	5,419,379	5,340,756
Equity securities	—	—	75,471	105,208
Total investment securities available for sale	\$4,858,178	\$4,783,507	\$7,229,014	\$7,180,180
Investment securities held to maturity				
Mortgage-backed securities held to maturity	\$2,299,774	\$2,302,093	\$76	\$81

There were no gross gains or losses on sales of investment securities available for sale for the three or six months ended June 30, 2018. Gross gains and gross losses on sales of investment securities available for sale were \$3.4 million and \$2 thousand, respectively for the three months ended June 30, 2017. Gross gains and gross losses on sales of investment securities available for sale were \$3.4 million and \$29 thousand, respectively for the six months ended June 30, 2017.

The following table provides the realized and unrealized gains or losses on marketable equity securities for the three and six months ended June 30, 2018.

(Dollars in thousands)	Three months ended June 30, 2018	Six months ended June 30, 2018
Marketable equity securities gains, net	\$4,440	\$5,411
Less net gains recognized on marketable equity securities sold	139	235
Unrealized gains recognized on marketable equity securities held	\$4,301	\$5,176

Table of Contents

The following table provides information regarding securities available for sale with unrealized losses as of June 30, 2018 and December 31, 2017.

(Dollars in thousands)	June 30, 2018					
	Less than 12 months	12 months or more	Total			
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Investment securities available for sale:						
U.S. Treasury	\$1,503,974	\$ 4,461	\$—	\$ —	\$1,503,974	\$ 4,461
Government agency	83,383	328	2,004	27	85,387	355
Mortgage-backed securities	1,923,954	50,765	654,212	21,107	2,578,166	71,872
Corporate bonds	24,673	248	5,025	2	29,698	250
Total	\$3,535,984	\$ 55,802	\$661,241	\$ 21,136	\$4,197,225	\$ 76,938
Investment securities held to maturity:						
Mortgage-backed securities	\$1,126,683	\$ 1,249	\$11,219	\$ 210	\$1,137,902	\$ 1,459
December 31, 2017						
	Less than 12 months	12 months or more	Total			
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Investment securities available for sale:						
U.S. Treasury	\$1,408,166	\$ 345	\$249,698	\$ 201	\$1,657,864	\$ 546
Government agency	848	12	2,527	28	3,375	40
Mortgage-backed securities	2,333,254	20,911	2,723,406	59,241	5,056,660	80,152
Corporate bonds	5,025	8	—	—	5,025	8
Other	5,349	182	—	—	5,349	182
Total	\$3,752,642	\$ 21,458	\$2,975,631	\$ 59,470	\$6,728,273	\$ 80,928

As of June 30, 2018, there were 120 investment securities available for sale that had continuous losses for more than 12 months of which 119 are government sponsored enterprise-issued mortgage-backed securities or government agency securities and 1 is a corporate bond. There were 2 investment securities held to maturity, which were government sponsored enterprise-issued mortgage securities, that had continuous losses for more than 12 months at June 30, 2018.

None of the unrealized losses identified as of June 30, 2018 or December 31, 2017 relate to the marketability of the securities or the issuers' ability to honor redemption obligations. Rather, the unrealized losses relate to changes in interest rates relative to when the debt securities were purchased. BancShares has the ability and intent to retain these securities for a period of time sufficient to recover all unrealized losses. Therefore, none of the securities were deemed to be other than temporarily impaired.

Debt securities having an aggregate carrying value of \$3.67 billion at June 30, 2018 and \$4.59 billion at December 31, 2017 were pledged as collateral to secure public funds on deposit and certain short-term borrowings, and for other purposes as required by law.

NOTE D - LOANS AND LEASES

BancShares' accounting methods for loans and leases differ depending on whether they are non-PCI or PCI. For loans to be included as non-PCI, they are either originated by FCB or it must be determined that the loans do not have any credit deterioration at the time of acquisition. Conversely, loans for which it is probable at acquisition that all required payments will not be collected in accordance with contractual terms are considered impaired and, therefore, classified as PCI loans. PCI loans are recorded at fair value at the date of acquisition. No allowance for loan and lease losses is recorded on the acquisition date as the fair value of the acquired assets incorporates assumptions regarding credit risk over the life of the loans. An allowance is subsequently recorded if there is additional credit deterioration after the acquisition date.

BancShares reports non-PCI and PCI loan portfolios separately, and the non-PCI portfolio is further divided into commercial and non-commercial based on the type of borrower, purpose, collateral, and/or our underlying credit management processes. Additionally, commercial and non-commercial loans are assigned to loan classes, which further disaggregate loans based upon common risk characteristics.

Table of Contents

Commercial – Commercial loan classes include construction and land development, commercial mortgage, other commercial real estate, commercial and industrial, lease financing and other.

Construction and land development – Construction and land development consists of loans to finance land for development, investment, and use in a commercial business enterprise; multifamily apartments; and other commercial buildings that may be owner-occupied or income generating investments for the owner.

Commercial mortgage – Commercial mortgage consists of loans to purchase or refinance owner-occupied nonresidential and investment properties. Investment properties include office buildings and other facilities that are rented or leased to unrelated parties.

Other commercial real estate – Other commercial real estate consists of loans secured by farmland (including residential farms and other improvements) and multifamily (5 or more) residential properties.

Commercial and industrial – Commercial and industrial consists of loans or lines of credit to finance corporate credit cards, accounts receivable, inventory and other general business purposes.

Lease financing – Lease financing consists solely of lease financing agreements for business equipment, vehicles and other assets.

Other – Other consists of all other commercial loans not classified in one of the preceding classes. These typically include loans to non-profit organizations such as churches, hospitals, educational and charitable organizations, and certain loans repurchased with government guarantees.

Noncommercial – Noncommercial loan classes consist of residential and revolving mortgage, construction and land development, and consumer loans.

Residential mortgage – Residential real estate consists of loans to purchase, construct or refinance the borrower's primary dwelling, second residence or vacation home.

Revolving mortgage – Revolving mortgage consists of home equity lines of credit that are secured by first or second liens on the borrower's primary residence.

Construction and land development – Construction and land development consists of loans to construct the borrower's primary or secondary residence or vacant land upon which the owner intends to construct a dwelling at a future date.

Consumer – Consumer loans consist of installment loans to finance purchases of vehicles, unsecured home improvements, student loans and revolving lines of credit that can be secured or unsecured, including personal credit cards.

Loans and leases outstanding included the following at June 30, 2018 and December 31, 2017:

(Dollars in thousands)	June 30, 2018	December 31, 2017
Non-PCI loans and leases:		
Commercial:		
Construction and land development	\$ 715,011	\$ 669,215
Commercial mortgage	10,278,741	9,729,022
Other commercial real estate	473,452	473,433
Commercial and industrial	3,097,541	2,730,407
Lease financing	613,377	894,801
Other	296,614	302,176
Total commercial loans	15,474,736	14,799,054
Noncommercial:		
Residential mortgage	3,980,845	3,523,786
Revolving mortgage	2,604,955	2,701,525
Construction and land development	250,704	248,289
Consumer	1,552,928	1,561,173

Total noncommercial loans	8,389,432	8,034,773
Total non-PCI loans and leases	23,864,168	22,833,827
PCI loans:		
Total PCI loans	674,269	762,998
Total loans and leases	\$ 24,538,437	\$ 23,596,825

Table of Contents

At June 30, 2018, \$9.08 billion in noncovered loans with a lendable collateral value of \$6.22 billion were used to secure \$128.7 million in Federal Home Loan Bank (FHLB) of Atlanta advances, resulting in additional borrowing capacity of \$6.09 billion. At December 31, 2017, \$8.75 billion in noncovered loans with a lendable collateral value of \$6.08 billion were used to secure \$835.2 million in FHLB of Atlanta advances, resulting in additional borrowing capacity of \$5.24 billion. At June 30, 2018, \$2.88 billion in noncovered loans with a lendable collateral value of \$2.17 billion were used to secure additional borrowing capacity at the Federal Reserve Bank (FRB). At December 31, 2017, \$2.77 billion in noncovered loans with a lendable collateral value of \$2.08 billion were used to secure additional borrowing capacity at the FRB.

Certain residential real estate loans are originated to be sold to investors and are recorded in loans held for sale at fair value. Loans held for sale totaled \$59.0 million and \$51.2 million at June 30, 2018 and December 31, 2017, respectively. In addition, we may change our strategy for certain portfolio loans and sell them in the secondary market. At that time, portfolio loans are transferred to loans held for sale at the lower of amortized cost or market. During the three and six months ended June 30, 2018, total proceeds from sales of loans held for sale were \$164.2 million and \$302.8 million, respectively, and there were no transfers to loans held for sale from the residential mortgage portfolio for either period. For the three months ended June 30, 2017, total proceeds from sales of loans held for sale which did not include any loans transferred from the residential mortgage portfolio were \$147.0 million. For the six months ended June 30, 2017, total proceeds from sales of loans held for sale were \$342.1 million of which \$32.3 million in sales were transferred to loans held for sale from the residential mortgage portfolio, resulting in a gain of \$164 thousand.

Net deferred fees on originated non-PCI loans and leases, including unearned income as well as unamortized costs and fees, were \$1.2 million and \$1.7 million at June 30, 2018 and December 31, 2017, respectively. The unamortized discount related to purchased non-PCI loans and leases in the HomeBancorp, Guaranty Bank (Guaranty), Cordia Bancorp Inc. (Cordia) and First Citizens Bancorporation, Inc. (Bancorporation) acquisitions was \$7.0 million, \$12.3 million, \$1.9 million and \$14.7 million, respectively, at June 30, 2018. At December 31, 2017, the unamortized discount related to purchased non-PCI loans and leases from the Guaranty, Cordia and Bancorporation acquisitions was \$14.2 million, \$2.7 million and \$18.1 million, respectively. During the three months ended June 30, 2018 and June 30, 2017, accretion income on purchased non-PCI loans and leases was \$4.1 million and \$3.0 million, respectively. During the six months ended June 30, 2018 and June 30, 2017, accretion income on purchased non-PCI loans and leases was \$7.0 million and \$6.0 million, respectively.

Credit quality indicators

Loans and leases are monitored for credit quality on a recurring basis. The credit quality indicators used are dependent on the portfolio segment to which the loan relates. Commercial and noncommercial loans and leases have different credit quality indicators as a result of the unique characteristics of the loan segment being evaluated. The credit quality indicators for non-PCI and PCI commercial loans and leases are developed through a review of individual borrowers on an ongoing basis. Commercial loans are evaluated periodically with more frequent evaluations done on more severely criticized loans or leases. The credit quality indicators for non-PCI and PCI noncommercial loans are based on the delinquency status of the borrower. As the borrower becomes more delinquent, the likelihood of loss increases. The indicators represent the rating for loans or leases as of the date presented based on the most recent assessment performed. These credit quality indicators are defined as follows:

Pass – A pass rated asset is not adversely classified because it does not display any of the characteristics for adverse classification.

Special mention – A special mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, such potential weaknesses may result in deterioration of the repayment prospects or collateral position at some future date. Special mention assets are not adversely classified and do not warrant adverse classification.

Substandard – A substandard asset is inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Assets classified as substandard generally have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. These assets are characterized by the distinct possibility of loss if the deficiencies are not corrected.

Doubtful – An asset classified as doubtful has all the weaknesses inherent in an asset classified substandard with the added characteristic that the weaknesses make collection or liquidation in full highly questionable and improbable on the basis of currently existing facts, conditions and values.

Loss – Assets classified as loss are considered uncollectible and of such little value that it is inappropriate to be carried as an asset. This classification is not necessarily equivalent to any potential for recovery or salvage value, but rather that it is not appropriate to defer a full charge-off even though partial recovery may be affected in the future.

Table of Contents

Ungraded – Ungraded loans represent loans that are not included in the individual credit grading process due to their relatively small balances or borrower type. The majority of ungraded loans at June 30, 2018 and December 31, 2017 relate to business credit cards. Business credit card loans are subject to automatic charge-off when they become 120 days past due in the same manner as unsecured consumer lines of credit. The remaining balance is comprised of a small amount of commercial mortgage, lease financing and other commercial real estate loans.

Non-PCI loans and leases outstanding at June 30, 2018 and December 31, 2017 by credit quality indicator are provided below:

June 30, 2018

(Dollars in thousands) Non-PCI commercial loans and leases

Grade:	Construction and land development	Commercial mortgage	Other commercial real estate	Commercial and industrial	Lease financing	Other	Total non-PCI commercial loans and leases
Pass	\$703,034	\$10,083,382	\$ 470,236	\$ 2,868,180	\$ 603,760	\$293,804	\$15,022,396
Special mention	352	88,157	1,159	35,636	3,916	1,258	130,478
Substandard	3,195	105,647	2,057	21,265	5,701	1,552	139,417
Doubtful	—	999	—	365	—	—	1,364
Ungraded	8,430	556	—	172,095	—	—	181,081
Total	\$715,011	\$10,278,741	\$ 473,452	\$ 3,097,541	\$ 613,377	\$296,614	\$15,474,736

December 31, 2017

Non-PCI commercial loans and leases

	Construction and land development	Commercial mortgage	Other commercial real estate	Commercial and industrial	Lease financing	Other	Total non-PCI commercial loans and leases
Pass	\$665,197	\$9,521,019	\$ 468,942	\$ 2,511,307	\$ 883,779	\$298,064	\$14,348,308
Special mention	691	78,643	1,260	44,130	4,340	2,919	131,983
Substandard	3,327	128,848	3,224	18,617	6,585	1,193	161,794
Doubtful	—	262	—	385	—	—	647
Ungraded	—	250	7	155,968	97	—	156,322
Total	\$669,215	\$9,729,022	\$ 473,433	\$ 2,730,407	\$ 894,801	\$302,176	\$14,799,054

June 30, 2018

Non-PCI noncommercial loans and leases

(Dollars in thousands)	Residential mortgage	Revolving mortgage	Construction and land development	Consumer	Total non-PCI noncommercial loans and leases
Current	\$3,936,065	\$2,581,818	\$ 248,343	\$1,541,465	\$ 8,307,691
30-59 days past due	21,032	9,864	1,839	6,013	38,748
60-89 days past due	6,291	3,367	51	2,729	12,438
90 days or greater past due	17,457	9,906	471	2,721	30,555
Total	\$3,980,845	\$2,604,955	\$ 250,704	\$1,552,928	\$ 8,389,432

December 31, 2017

Non-PCI noncommercial loans and leases

	Residential mortgage	Revolving mortgage	Construction and land development	Consumer	Total non-PCI noncommercial loans and leases
Current	\$3,465,935	\$2,674,390	\$ 239,648	\$1,546,473	\$ 7,926,446
30-59 days past due	27,886	13,428	7,154	8,812	57,280
60-89 days past due	8,064	3,485	108	2,893	14,550
90 days or greater past due	21,901	10,222	1,379	2,995	36,497
Total	\$3,523,786	\$2,701,525	\$ 248,289	\$1,561,173	\$ 8,034,773

Table of Contents

PCI loans outstanding at June 30, 2018 and December 31, 2017 by credit quality indicator are provided below:

	June 30, 2018	December 31, 2017
(Dollars in thousands) PCI commercial loans		
Grade:		
Pass	\$ 165,578	\$ 201,332
Special mention	58,024	63,257
Substandard	105,937	117,068
Doubtful	6,536	11,735
Ungraded	34	27
Total	\$ 336,109	\$ 393,419

	June 30, 2018	December 31, 2017
(Dollars in thousands) PCI noncommercial loans		
Current	\$ 299,579	\$ 318,632
30-59 days past due	12,146	13,343
60-89 days past due	4,167	6,212
90 days or greater past due	22,268	31,392
Total	\$ 338,160	\$ 369,579

The aging of the outstanding non-PCI loans and leases, by class, at June 30, 2018 and December 31, 2017 are provided in the tables below. Loans and leases 30 days or less past due are considered current as various grace periods allow borrowers to make payments within a stated period after the due date and still remain in compliance with the loan agreement.

	June 30, 2018					
(Dollars in thousands)	30-59 days past due	60-89 days past due	90 days or greater	Total past due	Current	Total loans and leases
Non-PCI loans and leases:						
Construction and land development - commercial	\$ 466	\$ 264	\$ 132	\$ 862	\$ 714,149	\$ 715,011
Commercial mortgage	10,120	5,021	5,599	20,740	10,258,001	10,278,741
Other commercial real estate	1,568	—	18	1,586	471,866	473,452
Commercial and industrial	6,445	3,743	1,155	11,343	3,086,198	3,097,541
Lease financing	3,062	1,167	951	5,180	608,197	613,377
Residential mortgage	21,032	6,291	17,457	44,780	3,936,065	3,980,845
Revolving mortgage	9,864	3,367	9,906	23,137	2,581,818	2,604,955
Construction and land development - noncommercial	1,839	51	471	2,361	248,343	250,704
Consumer	6,013	2,729	2,721	11,463	1,541,465	1,552,928
Other	42	17	—	59	296,555	296,614
Total non-PCI loans and leases	\$ 60,451	\$ 22,650	\$ 38,410	\$ 121,511	\$ 23,742,657	\$ 23,864,168

	December 31, 2017				Current	Total loans and leases
	30-59 days past due	60-89 days past due	90 days or greater	Total past due		
Non-PCI loans and leases:						

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Construction and land development - commercial	\$491	\$ 442	\$357	\$1,290	\$667,925	\$669,215
Commercial mortgage	12,288	2,375	6,490	21,153	9,707,869	9,729,022
Other commercial real estate	107	—	75	182	473,251	473,433
Commercial and industrial	6,694	1,510	1,266	9,470	2,720,937	2,730,407
Lease financing	2,983	167	973	4,123	890,678	894,801
Residential mortgage	27,886	8,064	21,901	57,851	3,465,935	3,523,786
Revolving mortgage	13,428	3,485	10,222	27,135	2,674,390	2,701,525
Construction and land development - noncommercial	7,154	108	1,379	8,641	239,648	248,289
Consumer	8,812	2,893	2,995	14,700	1,546,473	1,561,173
Other	188	6	133	327	301,849	302,176
Total non-PCI loans and leases	\$80,031	\$ 19,050	\$45,791	\$144,872	\$22,688,955	\$22,833,827

Table of Contents

The recorded investment, by class, in loans and leases on nonaccrual status, and loans and leases greater than 90 days past due and still accruing at June 30, 2018 and December 31, 2017 for non-PCI loans and leases, were as follows:

	June 30, 2018		December 31, 2017	
	Loans		Loans	
	Nonaccruing	and	Nonaccruing	and
(Dollars in thousands)	loans	leases >	loans	leases >
	and	90	and	90
	leases	days and	leases	days and
		accruing		accruing
Non-PCI loans and leases:				
Construction and land development - commercial	\$420	\$ —	\$1,040	\$ —
Commercial mortgage	18,457	839	22,625	397
Other commercial real estate	103	—	916	—
Commercial and industrial	3,168	319	2,884	428
Lease financing	1,755	—	1,992	—
Residential mortgage	35,173	—	38,942	—
Revolving mortgage	22,500	—	19,990	—
Construction and land development - noncommercial	1,012	—	1,989	—
Consumer	2,390	2,021	1,992	2,153
Other	77	—	164	—
Total non-PCI loans and leases	\$85,055	\$ 3,179	\$92,534	\$ 2,978

Purchased non-PCI loans and leases

The following table relates to purchased non-PCI loans acquired in the HomeBancorp transaction and provides the contractually required payments, estimate of contractual cash flows not expected to be collected and fair value of the acquired loans at the acquisition date.

(Dollars in thousands)	
Contractually required payments	\$710,876
Contractual cash flows not expected to be collected	\$9,845
Fair value at acquisition date	\$550,618

The recorded fair values of purchased non-PCI loans acquired in the HomeBancorp transaction as of the acquisition date are as follows:

(Dollars in thousands)	
Commercial:	
Construction and land development	\$525
Commercial mortgage	188,688
Other commercial real estate	55,183
Commercial and industrial	7,931
Total commercial loans	252,327
Noncommercial:	
Residential mortgage	296,273
Revolving mortgage	51
Consumer	1,967
Total noncommercial loans	298,291
Total non-PCI loans	\$550,618

Table of Contents

Purchased credit-impaired loans

The following table relates to PCI loans acquired in the HomeBancorp transaction and summarizes the contractually required payments, which include principal and interest, expected cash flows to be collected and the fair value of PCI loans at the acquisition date.

(Dollars in thousands)

Contractually required payments \$26,651

Cash flows expected to be collected \$19,697

Fair value of loans at acquisition \$15,555

The recorded fair values of PCI loans acquired in the HomeBancorp transaction as of the acquisition date are as follows:

(Dollars in thousands)

Commercial:

Commercial mortgage \$7,815

Commercial and industrial 423

Total commercial loans 8,238

Noncommercial:

Residential mortgage 7,317

Total noncommercial loans 7,317

Total PCI loans \$15,555

The following table provides changes in the carrying value of all PCI loans during the six months ended June 30, 2018 and June 30, 2017:

(Dollars in thousands)	2018	2017
Balance at January 1	\$762,998	\$809,169
Fair value of acquired loans	15,555	199,682
Accretion	32,188	39,798
Payments received and other changes, net	(136,472)	(153,786)
Balance at June 30	\$674,269	\$894,863
Unpaid principal balance at June 30	\$1,044,148	\$1,199,358

The carrying value of loans on the cost recovery method was \$2.1 million at June 30, 2018 and \$1.1 million at December 31, 2017. The cost recovery method is applied to loans when the timing of future cash flows is not reasonably estimable due to borrower nonperformance or uncertainty in the ultimate disposition of the asset. The recorded investment of PCI loans on nonaccrual status was \$1.6 million and \$624 thousand at June 30, 2018 and December 31, 2017, respectively.

During the three months ended June 30, 2018 and June 30, 2017, accretion income on PCI loans was \$14.2 million and \$20.4 million, respectively.

For PCI loans, improved credit loss expectations generally result in the reclassification of nonaccretable difference to accretable yield. Changes in expected cash flow not related to credit improvements or deterioration do not affect the nonaccretable difference.

The following table documents changes to the amount of accretable yield for the first six months of 2018 and 2017.

(Dollars in thousands)	2018	2017
Balance at January 1	\$316,679	\$335,074
Additions from acquisitions	4,142	44,120
Accretion	(32,188)	(39,798)
Reclassifications from nonaccretable difference	6,899	12,328

Changes in expected cash flows that do not affect nonaccretable difference	48,988	(1,405)
Balance at June 30	\$344,520	\$350,319

Table of Contents

NOTE E - ALLOWANCE FOR LOAN AND LEASE LOSSES (ALLL)

The following tables present the activity in the ALLL for non-PCI loan and lease losses by loan class for the three and six months ended June 30, 2018 and June 30, 2017:

Three months ended June 30, 2018

(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage real estate	Other commercial and industrial	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer	Total
Non-PCI Loans Allowance for loan and lease losses:											
Balance at April 1	\$26,718	\$43,833	\$3,423	\$53,016	\$6,301	\$4,842	\$16,489	\$22,104	\$3,913	\$30,181	\$210,820
Provision	(3,139)	866	468	5,670	(1,879)	(114)	1,492	289	50	4,574	8,277
Charge-offs	(8)	(459)	(69)	(1,994)	(445)	(38)	(289)	(1,027)	(37)	(5,312)	(9,678)
Recoveries	93	225	1	638	4	1	110	520	101	1,330	3,023
Balance at June 30	\$23,664	\$44,465	\$3,823	\$57,330	\$3,981	\$4,691	\$17,802	\$21,886	\$4,027	\$30,773	\$212,442

Three months ended June 30, 2017

(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage real estate	Other commercial and industrial	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer	Total
Balance at April 1	\$31,391	\$48,611	\$3,572	\$50,829	\$6,315	\$3,534	\$15,835	\$21,290	\$1,513	\$27,129	\$210,019
Provision	2,372	639	33	968	186	(214)	155	1,054	(10)	4,569	9,752
Charge-offs	(413)	(235)	—	(3,121)	(97)	(64)	(222)	(280)	—	(4,991)	(9,423)
Recoveries	209	731	7	2,392	—	46	75	401	—	1,093	4,954
Balance at June 30	\$33,559	\$49,746	\$3,612	\$51,068	\$6,404	\$3,302	\$15,843	\$22,465	\$1,503	\$27,800	\$215,302

Six months ended June 30, 2018

(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage real estate	Other commercial and industrial	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer	Total
Balance at January 1	\$24,470	\$45,005	\$4,571	\$53,697	\$6,127	\$4,689	\$15,706	\$22,436	\$3,962	\$31,204	\$211,867

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Provision	(914)	(499)	(825)	5,245	(892)	—	3,004	755	157	7,497	13,528							
Charge-offs	(8)	(505)	(69)	(3,469)	(1,299)	(41)	(1,095)	(2,019)	(219)	(10,567)	(19,291)
Recoveries	116		464		146		1,857		45		43		187		714		127		2,639		6,338	
Balance at June 30	\$23,664		\$44,465		\$3,823		\$57,330		\$3,981		\$4,691		\$17,802		\$21,886		\$4,027		\$30,773		\$212,442	

Six months ended June 30, 2017

(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage	Other commercial real estate	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer	Total
Balance at January 1	\$28,877	\$48,278	\$3,269	\$50,225	\$5,907	\$3,127	\$14,447	\$21,013	\$1,596	\$28,287	\$205,026
Provision	4,908	645	337	4,560	761	241	1,506	1,604	(93)	6,359	20,828
Charge-offs	(490)	(272)	(5)	(6,374)	(270)	(187)	(472)	(1,105)	—	(9,019)	(18,194)
Recoveries	264	1,095	11	2,657	6	121	362	953	—	2,173	7,642
Balance at June 30	\$33,559	\$49,746	\$3,612	\$51,068	\$6,404	\$3,302	\$15,843	\$22,465	\$1,503	\$27,800	\$215,302

Table of Contents

The following tables present the allowance for non-PCI loan and lease losses and the recorded investment in loans, by loan class, based on impairment method as of June 30, 2018 and December 31, 2017:

	June 30, 2018									
(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage	Other commercial real estate	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer
Allowance for loan and lease losses:										
ALLL for loans and leases individually evaluated for impairment	\$274	\$3,325	\$65	\$985	\$107	\$20	\$3,343	\$1,112	\$66	\$704
ALLL for loans and leases collectively evaluated for impairment	23,390	41,140	3,758	56,345	3,874	4,671	14,459	20,774	3,961	30,069
Total allowance for loan and lease losses	\$23,664	\$44,465	\$3,823	\$57,330	\$3,981	\$4,691	\$17,802	\$21,886	\$4,027	\$30,773
Loans and leases:										
Loans and leases individually evaluated for impairment	\$2,098	\$66,172	\$1,077	\$7,652	\$1,176	\$97	\$43,953	\$27,407	\$2,911	\$2,685
Loans and leases collectively evaluated for impairment	712,913	10,212,569	472,375	3,089,889	612,201	296,517	3,936,892	2,577,548	247,793	1,550,243
Total loan and leases	\$715,011	\$10,278,741	\$473,452	\$3,097,541	\$613,377	\$296,614	\$3,980,845	\$2,604,955	\$250,704	\$1,552,928
	December 31, 2017									
(Dollars in thousands)	Construction and land development - commercial	Commercial mortgage	Other commercial real estate	Commercial and industrial	Lease financing	Other	Residential mortgage	Revolving mortgage	Construction and land development - non-commercial	Consumer

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	development - commercial		real estate	industrial						development - non-commercial	
Allowance for loan and lease losses: ALLL for loans and leases individually evaluated for impairment	\$185	\$3,648	\$209	\$665	\$397	\$—	\$2,733	\$1,085	\$68	\$738	
ALLL for loans and leases collectively evaluated for impairment	24,285	41,357	4,362	53,032	5,730	4,689	12,973	21,351	3,894	30,466	
Total allowance for loan and lease losses	\$24,470	\$45,005	\$4,571	\$53,697	\$6,127	\$4,689	\$15,706	\$22,436	\$3,962	\$31,204	
Loans and leases: Loans and leases individually evaluated for impairment	\$788	\$73,655	\$1,857	\$7,974	\$1,914	\$521	\$37,842	\$23,770	\$4,551	\$2,774	
Loans and leases collectively evaluated for impairment	668,427	9,655,367	471,576	2,722,433	892,887	301,655	3,485,944	2,677,755	243,738	1,558,399	
Total loan and leases	\$669,215	\$9,729,022	\$473,433	\$2,730,407	\$894,801	\$302,176	\$3,523,786	\$2,701,525	\$248,289	\$1,561,173	

Table of Contents

The following tables show the activity in the allowance for PCI loan losses for the three and six months ended June 30, 2018 and June 30, 2017.

(Dollars in thousands)	Three months ended June 30, 2018	Three months ended June 30, 2017
PCI Loans		
Allowance for loan and lease losses:		
Balance at April 1	\$12,296	\$10,924
Provision	161	2,572
Charge-offs	(34)	—
Recoveries	—	—
Balance at June 30	\$12,423	\$13,496
	Six months ended June 30, 2018	Six months ended June 30, 2017
Balance at January 1	\$10,026	\$13,769
Provision	2,515	(273)
Charge-offs	(118)	—
Recoveries	—	—
Balance at June 30	\$12,423	\$13,496

The following table shows the ending balances of PCI loans and related allowance as of June 30, 2018 and December 31, 2017:

(Dollars in thousands)	June 30, 2018	December 31, 2017
ALLL for loans acquired with deteriorated credit quality	\$12,423	\$ 10,026
Loans acquired with deteriorated credit quality	674,269	762,998
As of June 30, 2018 and December 31, 2017, \$160.8 million and \$279.8 million, respectively, in PCI loans experienced an adverse change in expected cash flows since the date of acquisition.		

Table of Contents

The following tables provide information on non-PCI impaired loans and leases individually evaluated as of June 30, 2018 and December 31, 2017.

	June 30, 2018				
(Dollars in thousands)	With a recorded allowance	With no recorded allowance	Total	Unpaid principal balance	Related allowance recorded
Non-PCI impaired loans and leases:					
Construction and land development - commercial	\$2,098	\$ —	\$2,098	\$2,431	\$ 274
Commercial mortgage	35,934	30,238	66,172	72,467	3,325
Other commercial real estate	375	702	1,077	1,264	65
Commercial and industrial	6,262	1,390	7,652	11,684	985
Lease financing	789	387	1,176	2,808	107
Other	97	—	97	315	20
Residential mortgage	25,529	18,424	43,953	46,684	3,343
Revolving mortgage	10,217	17,190	27,407	30,170	1,112
Construction and land development - noncommercial	544	2,367	2,911	3,633	66
Consumer	1,777	908	2,685	3,004	704
Total non-PCI impaired loans and leases	\$83,622	\$ 71,606	\$ 155,228	\$ 174,460	\$ 10,001

(Dollars in thousands)	December 31, 2017			Unpaid principal balance	Related allowance recorded
	With a recorded allowance	With no recorded allowance	Total		
Non-PCI impaired loans and leases:					
Construction and land development - commercial	\$788	\$ —	\$788	\$1,110	\$ 185
Commercial mortgage	39,135	34,520	73,655	78,936	3,648
Other commercial real estate	1,351	506	1,857	2,267	209
Commercial and industrial	6,326	1,648	7,974	10,475	665
Lease financing	1,890	24	1,914	2,571	397
Other	—	521	521	521	—
Residential mortgage	19,135	18,707	37,842	39,946	2,733
Revolving mortgage	5,875	17,895	23,770	25,941	1,085
Construction and land development - noncommercial	592	3,959	4,551	5,224	68
Consumer	2,107	667	2,774	3,043	738
Total non-PCI impaired loans and leases	\$77,199	\$ 78,447	\$ 155,646	\$ 170,034	\$ 9,728

Non-PCI impaired loans less than \$500,000 that are collectively evaluated were \$44.1 million and \$49.1 million at June 30, 2018 and December 31, 2017, respectively.

Table of Contents

The following tables show the average non-PCI impaired loan balance and the interest income recognized by loan class for the three and six months ended June 30, 2018 and June 30, 2017:

	Three months ended June 30, 2018		Three months ended June 30, 2017	
(Dollars in thousands)	Average balance	Interest income recognized	Average balance	Interest income recognized
Non-PCI impaired loans and leases:				
Construction and land development - commercial	\$1,485	\$ 17	\$970	\$ 11
Commercial mortgage	68,113	659	74,121	651
Other commercial real estate	1,345	12	1,525	9
Commercial and industrial	7,585	76	10,159	98
Lease financing	1,842	14	1,911	14
Other	67	—	434	5
Residential mortgage	42,046	298	36,767	272
Revolving mortgage	26,388	222	8,484	62
Construction and land development - noncommercial	3,526	44	3,185	33
Consumer	2,654	28	2,052	24
Total non-PCI impaired loans and leases	\$155,051	\$ 1,370	\$139,608	\$ 1,179

	Six months ended June 30, 2018		Six months ended June 30, 2017	
(Dollars in thousands)	Average balance	Interest income recognized	Average balance	Interest income recognized
Non-PCI impaired loans and leases:				
Construction and land development - commercial	\$1,320	\$ 28	\$1,013	\$ 23
Commercial mortgage	70,190	1,370	74,715	1,293
Other commercial real estate	1,529	23	1,555	17
Commercial and industrial	7,554	152	10,844	202
Lease financing	2,040	25	1,740	28
Other	34	—	315	7
Residential mortgage	40,385	573	34,864	525
Revolving mortgage	25,590	423	8,227	119
Construction and land development - noncommercial	3,815	92	2,895	66
Consumer	2,581	56	1,976	47
Total non-PCI impaired loans and leases	\$155,038	\$ 2,742	\$138,144	\$ 2,327

Table of Contents

Troubled Debt Restructurings

BancShares accounts for certain loan modifications or restructurings as troubled debt restructurings (TDRs). In general, the modification or restructuring of a loan is considered a TDR if, for economic reasons or legal reasons related to a borrower's financial difficulties, a concession is granted to the borrower that creditors would not otherwise consider. Concessions may relate to the contractual interest rate, maturity date, payment structure or other actions. The majority of TDRs are included in the special mention, substandard or doubtful credit grading categories, which results in more elevated loss expectations when projecting the expected cash flows that are used to determine the allowance for loan losses associated with these loans. The more severely graded the loan, the lower the estimated expected cash flows and the greater the allowance recorded. All TDRs are individually evaluated for impairment through review of collateral values or analysis of cash flows at least annually.

The following table provides a summary of total TDRs by accrual status.

(Dollars in thousands)	June 30, 2018			December 31, 2017		
	Accruing	Nonaccruing	Total	Accruing	Nonaccruing	Total
Commercial loans						
Construction and land development - commercial	\$2,050	\$ 228	\$2,278	\$4,089	\$ 483	\$4,572
Commercial mortgage	58,877	10,304	69,181	62,358	15,863	78,221
Other commercial real estate	1,039	39	1,078	1,012	788	1,800
Commercial and industrial	6,673	988	7,661	7,598	910	8,508
Lease financing	677	429	1,106	722	1,048	1,770
Other	44	126	170	521	—	521
Total commercial TDRs	69,360	12,114	81,474	76,300	19,092	95,392
Noncommercial						
Residential mortgage	38,266	9,958	48,224	34,067	9,475	43,542
Revolving mortgage	19,752	6,778	26,530	17,673	5,180	22,853
Construction and land development - noncommercial	2,821	90	2,911	—	—	—
Consumer and other	2,111	574	2,685	2,351	423	2,774
Total noncommercial TDRs	62,950	17,400	80,350	54,091	15,078	69,169
Total TDRs	\$132,310	\$ 29,514	\$161,824	\$130,391	\$ 34,170	\$164,561

The following table shows the accrual status of non-PCI and PCI TDRs.

(Dollars in thousands)	June 30, 2018	December 31, 2017
Accruing TDRs:		
PCI	\$18,546	\$ 18,163
Non-PCI	113,764	112,228
Total accruing TDRs	132,310	130,391
Nonaccruing TDRs:		
PCI	253	272
Non-PCI	29,261	33,898
Total nonaccruing TDRs	29,514	34,170
All TDRs:		
PCI	18,799	18,435
Non-PCI	143,025	146,126
Total TDRs	\$161,824	\$ 164,561

Table of Contents

The following table provides the types of non-PCI and PCI TDRs made during the three and six months ended June 30, 2018 and June 30, 2017, as well as a summary of loans that were modified as a TDR during the twelve month periods ended June 30, 2018 and June 30, 2017 that subsequently defaulted during the three and six months ended June 30, 2018 and June 30, 2017. BancShares defines payment default as movement of the TDR to nonaccrual status, which is generally 90 days past due for TDRs, foreclosure or charge-off, whichever occurs first.

(Dollars in thousands)	Three months ended June 30, 2018		Three months ended June 30, 2017	
	All restructurings	Restructurings with payment default	All restructurings	Restructurings with payment default
	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end
Non-PCI and PCI loans and leases				
Interest only	1 154	2 821	3 571	1 332
Loan term extension	10 936	7 341	13 1,397	1 32
Below market interest rate	53 9,525	33 1,702	73 4,440	32 2,800
Discharged from bankruptcy	37 2,472	24 1,490	40 1,442	24 615
Total non-PCI and PCI restructurings	101 \$ 13,087	66 \$ 4,354	129 \$ 7,850	58 \$ 3,779
(Dollars in thousands)	Six months ended June 30, 2018		Six months ended June 30, 2017	
	All restructurings	Restructurings with payment default	All restructurings	Restructurings with payment default
	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end	Number of Loans Recorded investment at period end
Non-PCI and PCI loans and leases				
Interest only	2 821	2 821	3 571	1 332
Loan term extension	17 1,658	8 638	21 2,070	1 32
Below market interest rate	139 15,873	64 3,385	159 12,582	49 4,231
Discharged from bankruptcy	91 5,595	55 4,338	97 3,005	42 2,091
Total non-PCI and PCI restructurings	249 \$ 23,947	129 \$ 9,182	280 \$ 18,228	93 \$ 6,686

For the three and six months ended June 30, 2018 and June 30, 2017, the pre-modification and post-modification outstanding recorded investments of loans modified as TDRs were not materially different.

Table of Contents

NOTE F - OTHER REAL ESTATE OWNED (OREO)

The following table explains changes in other real estate owned during the six months ended June 30, 2018 and June 30, 2017.

(Dollars in thousands)	Total
Balance at December 31, 2016	\$61,231
Additions	21,891
Additions acquired in the Guaranty Bank acquisition	55
Sales	(20,236)
Write-downs	(2,160)
Balance at June 30, 2017	\$60,781

Balance at December 31, 2017	\$51,097
Additions	11,868
Additions acquired in the HomeBanc acquisition	2,135
Sales	(15,769)
Write-downs	(2,698)
Balance at June 30, 2018	\$46,633

At June 30, 2018 and December 31, 2017, BancShares had \$15.1 million and \$19.8 million, respectively, of foreclosed residential real estate property in OREO. The recorded investment in consumer mortgage loans collateralized by residential real estate property in the process of foreclosure was \$25.3 million and \$26.9 million at June 30, 2018 and December 31, 2017, respectively.

NOTE G - FDIC SHARED-LOSS PAYABLE

BancShares completed six FDIC-assisted transactions with shared-loss agreements during the period beginning in 2009 through 2011. Prior to its merger into BancShares, Bancorporation completed three FDIC-assisted transactions with shared-loss agreements.

As of June 30, 2018, shared-loss agreements are still active for Georgian Bank (GB) and United Western Bank (UWB). Shared-loss protection remains for single family residential loans acquired from UWB and GB in the amount of \$62.1 million.

The shared-loss agreements for two FDIC-assisted transactions, First Regional Bank (FRB) and UWB, include provisions related to payments that may be owed to the FDIC at the termination of the agreements (clawback liability). The clawback liability represents a payment by BancShares to the FDIC if actual cumulative losses on acquired covered assets are lower than the cumulative losses originally estimated by the FDIC at the time of acquisition and is recorded in the Consolidated Balance Sheets as a payable to the FDIC under the relevant shared-loss agreements. As of June 30, 2018 and December 31, 2017, the estimated clawback liability was \$103.5 million and \$101.3 million, respectively. The clawback liability payment dates for FRB and UWB are March 2020 and March 2021, respectively.

The following table provides changes in the FDIC shared-loss payable for the three and six months ended June 30, 2018 and June 30, 2017.

	Three months ended June 30		Six months ended June 30	
(Dollars in thousands)	2018	2017	2018	2017
Beginning balance	\$102,466	\$98,013	\$101,342	\$97,008
Amortization	1,001	963	1,993	1,917
Adjustments related to changes in assumptions	20	150	152	201
Ending balance	\$103,487	\$99,126	\$103,487	\$99,126

NOTE H - MORTGAGE SERVICING RIGHTS

Our portfolio of residential mortgage loans serviced for third parties was \$2.87 billion and \$2.81 billion as of June 30, 2018 and December 31, 2017, respectively. These loans were originated by BancShares and sold to third parties on a non-recourse basis with servicing rights retained. These retained servicing rights are recorded as a servicing asset and reported in other intangible assets on the Consolidated Balance Sheets. The mortgage servicing rights are initially recorded at fair value and then carried at the lower of amortized cost or fair market value.

Table of Contents

The activity of the servicing asset for the three and six months ended June 30, 2018 and 2017 is presented in the following table:

	Three months ended June 30		Six months ended June 30	
(Dollars in thousands)	2018	2017	2018	2017
Beginning balance	\$21,659	\$20,771	\$21,945	\$20,415
Servicing rights originated	1,430	1,123	2,630	2,825
Amortization	(1,432)	(1,370)	(2,918)	(2,720)
Valuation allowance reversal	—	—	—	4
Ending balance	\$21,657	\$20,524	\$21,657	\$20,524

The amortization expense related to mortgage servicing rights is included as a reduction of mortgage income in the Consolidated Statements of Income. Mortgage income for the three and six months ended June 30, 2018 and the three months ended June 30, 2017 did not include any impairment compared to an impairment reversal of \$4 thousand for the six months ended June 30, 2017.

Contractually specified mortgage servicing fees, late fees, and ancillary fees earned for both the three months ended June 30, 2018 and 2017 were \$1.9 million and reported in mortgage income in the Consolidated Statements of Income. For the six months ended June 30, 2018 and 2017, contractually specified mortgage servicing fees, late fees and ancillary fees earned were \$3.8 million and \$3.6 million, respectively.

Valuation of mortgage servicing rights is performed using a pooling methodology. Similar loans are pooled together and evaluated on a discounted earnings basis to determine the present value of future earnings. Key economic assumptions used to value mortgage servicing rights as of June 30, 2018 and December 31, 2017 were as follows:

	June 30, 2018		December 31, 2017	
Discount rate - conventional fixed loans	9.86	%	9.41	%
Discount rate - all loans excluding conventional fixed loans	10.86	%	10.41	%
Weighted average constant prepayment rate	8.43	%	10.93	%
Weighted average cost to service a loan	\$72.79		\$ 64.03	

The discount rate is based on the 10-year U.S. Treasury rate plus 700 basis points for conventional fixed loans and 800 basis points for all other loans. The 700 and 800 basis points are used as a risk premium when calculating the discount rate. The repayment rate is derived from the Public Securities Association Standard Prepayment model. The average cost to service a loan is based on the number of loans serviced and the total costs to service the loans.

NOTE I - REPURCHASE AGREEMENTS

BancShares utilizes securities sold under agreements to repurchase to facilitate the needs of customers and secure wholesale funding needs. Repurchase agreements are transactions whereby BancShares offers to sell to a counterparty an undivided interest in an eligible security at an agreed upon purchase price, and which obligates BancShares to repurchase the security on an agreed upon date at an agreed upon repurchase price plus interest at an agreed upon rate. Securities sold under agreements to repurchase are recorded at the amount of cash received in connection with the transaction and are generally reflected as short-term borrowings on the Consolidated Balance Sheets.

BancShares monitors collateral levels on a continuous basis and maintains records of each transaction specifically describing the applicable security and the counterparty's fractional interest in that security, and segregates the security from general assets in accordance with regulations governing custodial holdings of securities. The primary risk with repurchase agreements is market risk associated with the investments securing the transactions, as additional collateral may be required based on fair value changes of the underlying investments. Securities pledged as collateral under repurchase agreements are maintained with safekeeping agents. The carrying value of available for sale investment securities pledged as collateral under repurchase agreements was \$511.8 million and \$684.2 million at June 30, 2018 and December 31, 2017, respectively.

The remaining contractual maturity of the securities sold under agreements to repurchase by class of collateral pledged included overnight and continuous U.S. Treasury securities totaling \$499.7 million at June 30, 2018 and \$556.2

million at December 31, 2017. At December 31, 2017, there also were U.S. Treasury securities with a remaining contractual maturity of 30-90 days totaling \$30.0 million for a gross amount of \$586.2 million.

Table of Contents

NOTE J - ESTIMATED FAIR VALUES

Fair value estimates are intended to represent the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. Where there is no active market for a financial instrument, BancShares has made estimates using discounted cash flows or other valuation techniques. Inputs used in these valuation techniques are subjective in nature, involve uncertainties and require significant judgment and therefore can only be derived within a range of precision. Accordingly, the derived fair value estimates presented below are not necessarily indicative of the amounts BancShares would realize in a current market exchange.

ASC 820, Fair Value Measurements and Disclosures, indicates that assets and liabilities are recorded at fair value according to a fair value hierarchy comprised of three levels. The levels are based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. The level within the fair value hierarchy for an asset or liability is based on the highest level of input that is significant to the fair value measurement (with Level 1 considered highest and Level 3 considered lowest). A brief description of each level follows:

Level 1 values are based on quoted prices for identical instruments in active markets.

Level 2 values are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 values are derived from valuation techniques in which one or more significant inputs or assumptions are not observable in the market. These unobservable inputs and assumptions reflect estimates that market participants would use in pricing the asset or liability. Valuation techniques include the use of discounted cash flow models and similar techniques.

BancShares' management reviews any changes to its valuation methodologies to ensure they are appropriate and supportable, and refines valuation methodologies as more market-based data becomes available. Transfers between levels of the fair value hierarchy are recognized at the end of the reporting period.

The methodologies used to estimate the fair value of financial assets and financial liabilities are discussed below:

Investment securities available for sale. Investment securities available for sale are carried at fair value. U.S. Treasury, government agency and mortgage-backed securities are generally measured at fair value using a third party pricing service. The third party provider evaluates securities based on comparable investments with trades and market data and will utilize pricing models that use a variety of inputs, such as benchmark yields, reported trades, broker-dealer quotes, issuer spreads, benchmark securities, bids and offers as needed. These securities are generally classified as Level 2. Corporate bonds and trust preferred securities are generally measured at fair value based on indicative bids from broker-dealers and are not directly observable. These securities are considered Level 3.

Marketable equity securities. Equity securities are measured at fair value using observable closing prices and the valuation also considers the amount of market activity by examining the trade volume of each security. Equity securities are classified as Level 1 if they are traded in an active market and as Level 2 if the observable closing price is from a less than active market.

Loans held for sale. Certain residential real estate loans are originated to be sold to investors are carried at fair value based on quoted market prices for similar types of loans. Accordingly, the inputs used to calculate fair value of originated residential real estate loans held for sale are classified as Level 2 inputs. Portfolio loans that are subsequently transferred to held for sale to be sold in the secondary market are carried at the lower of amortized cost or fair value. The fair value of the transferred portfolio loans is based on the quoted prices and is considered a Level 1 input.

Net loans and leases (PCI and Non-PCI). Fair value is estimated based on discounted future cash flows using the current interest rates at which loans with similar terms would be made to borrowers of similar credit quality. The inputs used in the fair value measurements for loans and leases are considered Level 3 inputs.

FHLB stock. The carrying amount of FHLB stock is a reasonable estimate of fair value as these securities are not readily marketable and are evaluated for impairment based on the ultimate recoverability of the par value. BancShares considers positive and negative evidence, including the profitability and asset quality of the issuer, dividend payment history and recent redemption experience, when determining the ultimate recoverability of the par value. BancShares believes its investment in FHLB stock is ultimately recoverable at par. The inputs used in the fair value measurement for the FHLB stock are considered Level 2 inputs.

Table of Contents

Mortgage servicing rights. Mortgage servicing rights are carried at the lower of amortized cost or market and are, therefore, carried at fair value only when fair value is less than the amortized cost. The fair value of mortgage servicing rights is performed using a pooling methodology. Similar loans are pooled together and a model that relies on discount rates, estimates of prepayment rates and the weighted average cost to service the loans is used to determine the fair value. The inputs used in the fair value measurement for mortgage servicing rights are considered Level 3 inputs.

Deposits. For non-time deposits, carrying value is a reasonable estimate of fair value. The fair value of time deposits is estimated by discounting future cash flows using the interest rates currently offered for deposits of similar remaining maturities. The inputs used in the fair value measurement for deposits are considered Level 2 inputs.

Long-term obligations. For long-term obligations, the fair values are determined based on recent trades or sales of the actual security if available, otherwise, fair values are estimated by discounting future cash flows using current interest rates for similar financial instruments. The inputs used in the fair value measurement for long-term obligations are considered Level 2 inputs.

Payable to the FDIC for shared-loss agreements. The fair value of the payable to the FDIC for shared-loss agreements is determined by the projected cash flows based on expected payments to the FDIC in accordance with the shared-loss agreements. Cash flows are discounted using current discount rates to reflect the timing of the estimated amounts due to the FDIC. The inputs used in the fair value measurement for the payable to the FDIC are considered Level 3 inputs.

Off-balance-sheet commitments and contingencies. Carrying amounts are reasonable estimates of the fair values for such financial instruments. Carrying amounts include unamortized fee income and, in some cases, reserves for any credit losses from those financial instruments. These amounts are not material to BancShares' financial position.

For all other financial assets and financial liabilities, the carrying value is a reasonable estimate of the fair value as of June 30, 2018 and December 31, 2017. The carrying value and fair value for these assets and liabilities are equivalent because they are relatively short term in nature and there is no interest rate or credit risk that would cause the fair value to differ from the carrying value. Cash and due from banks is classified on the fair value hierarchy as Level 1. Overnight investments, income earned not collected, short-term borrowings and accrued interest payable are considered Level 2.

The table presents the carrying values and estimated fair values for financial instruments as of June 30, 2018 and December 31, 2017.

(Dollars in thousands)	June 30, 2018		December 31, 2017	
	Carrying value	Fair value	Carrying value	Fair value
Cash and due from banks	\$260,525	\$ 260,525	\$336,150	\$ 336,150
Overnight investments	1,223,311	1,223,311	1,387,927	1,387,927
Investment securities available for sale	4,783,507	4,783,507	7,180,180	7,180,180
Investment securities held to maturity	2,299,774	2,302,093	76	81
Marketable equity securities	107,264	107,264	—	—
Loans held for sale	58,961	58,961	51,179	51,179
Net loans and leases	24,313,572	23,704,523	23,374,932	22,257,803
Income earned not collected	99,567	99,567	95,249	95,249
Federal Home Loan Bank stock	22,658	22,658	52,685	52,685
Mortgage servicing rights	21,657	28,668	21,945	26,170
Deposits	30,408,884	30,362,605	29,266,275	29,230,768
Short-term borrowings	613,993	613,993	693,807	693,807

Long-term obligations	241,360	250,823	870,240	852,112
Payable to the FDIC for shared-loss agreements	103,487	103,966	101,342	102,684
Accrued interest payable	1,909	1,909	3,952	3,952

Table of Contents

Among BancShares' assets and liabilities, investment securities available for sale, marketable equity securities and loans held for sale are reported at their fair values on a recurring basis. For assets and liabilities carried at fair value on a recurring basis, the following table provides fair value information as of June 30, 2018 and December 31, 2017.

June 30, 2018

(Dollars in thousands)	Fair value	Fair value measurements using:		
		Level 1 inputs	Level 2 inputs	Level 3 inputs
Assets measured at fair value				
Investment securities available for sale				
U.S. Treasury	\$1,503,974	\$—	\$1,503,974	\$—
Government agency	131,035	—	131,035	—
Mortgage-backed securities	3,034,065	—	3,034,065	—
Corporate bonds	108,790	—	—	108,790
Other	5,643	—	—	5,643
Total investment securities available for sale	\$4,783,507	\$—	\$4,669,074	\$114,433
Marketable equity securities	\$107,264	\$21,667	\$85,597	\$—
Loans held for sale	\$58,961	\$—	\$58,961	\$—

December 31, 2017

(Dollars in thousands)	Fair value	Fair value measurements using:		
		Level 1 inputs	Level 2 inputs	Level 3 inputs
Assets measured at fair value				
Investment securities available for sale				
U.S. Treasury	\$1,657,864	\$—	\$1,657,864	\$—
Government agency	8,670	—	8,670	—
Mortgage-backed securities	5,340,756	—	5,340,756	—
Equity securities	105,208	19,341	85,867	—
Corporate bonds	59,963	—	59,963	—
Other	7,719	—	7,719	—
Total investment securities available for sale	\$7,180,180	\$19,341	\$7,160,839	\$—
Loans held for sale	\$51,179	\$—	\$51,179	\$—

During the three months ended June 30, 2018, there were no transfers between levels. For the six months ended June 30, 2018, there were transfers from Level 2 to Level 3 of \$59.7 million and \$5.6 million of corporate bonds and other investment securities available for sale, respectively. The transfers were due to a lack of observable inputs and trade activity for those securities. There were no transfers between levels for the three and six months ended June 30, 2017.

The following tables summarize activity for Level 3 assets:

(Dollars in thousands)	Three months ended June 30, 2018	
	Corporate bonds	Other
Balance at April 1, 2018	\$59,653	\$5,618
Amounts included in net income	48	7
Unrealized net (losses) gains included in other comprehensive income	(97)	18
Purchases	51,591	—

Sales	(2,405)	—
Balance at June 30, 2018	\$ 108,790	\$ 5,643

	Six months ended June 30, 2018	
(Dollars in thousands)	Corporate bonds	Other
Balance at January 1, 2018	\$—	\$—
Transfers in	59,653	5,618
Amounts included in net income	48	7
Unrealized net (losses) gains included in other comprehensive income	(97)	18
Purchases	51,591	—
Sales	(2,405)	—
Balance at June 30, 2018	\$ 108,790	\$ 5,643

Table of Contents

The following table presents quantitative information about Level 3 fair value measurements for fair value on a recurring basis at June 30, 2018.

(Dollars in thousands)			June 30, 2018 Fair Value
Level 3 assets	Valuation technique	Significant unobservable input	
Corporate bonds	Indicative bid provided by broker	Multiple factors, including but not limited to, current operations, financial condition, cash flows, and recently executed financing transactions related to the company	\$ 108,790
Other	Indicative bid provided by broker	Multiple factors, including but not limited to, current operations, financial condition, cash flows, and recently executed financing transactions related to the company	5,643

Fair Value Option

BancShares has elected the fair value option for residential real estate loans originated to be sold. This election reduces certain timing differences in the Consolidated Statement of Income and better aligns with the management of the portfolio from a business perspective. The changes in fair value are recorded as a component of mortgage income and included gains of \$700 thousand and \$291 thousand for the three months ended June 30, 2018 and June 30, 2017, respectively. For the six months ended June 30, 2018 and 2017, the changes in fair value were gains of \$245 thousand and \$3.5 million, respectively.

The following table summarizes the difference between the aggregate fair value and the aggregate unpaid principal balance for residential real estate originated for sale measured at fair value as of June 30, 2018 and December 31, 2017.

June 30, 2018			
(Dollars in thousands)	Fair Value	Aggregate Unpaid Principal Balance	Difference
Originated loans held for sale	\$58,961	\$ 57,334	\$ 1,627

December 31, 2017			
	Fair Value	Aggregate Unpaid Principal Balance	Difference
Originated loans held for sale	\$51,179	\$ 49,796	\$ 1,383

No originated loans held for sale were 90 or more days past due or on nonaccrual status as of June 30, 2018 or December 31, 2017.

Certain other assets are adjusted to their fair value on a nonrecurring basis, including impaired loans, OREO, and goodwill, which are periodically tested for impairment, and mortgage servicing rights, which are carried at the lower of amortized cost or market. Non-impaired loans held for investment, deposits, short-term borrowings and long-term obligations are not reported at fair value.

Impaired loans are deemed to be at fair value if an associated allowance or current period charge-off has been recorded. The value of impaired loans is determined by either collateral valuations or discounted present value of the expected cash flow calculations. Collateral values are determined using appraisals or other third-party value estimates of the subject property with discounts generally between 6 and 11 percent applied for estimated holding and selling costs and other external factors that may impact the marketability of the property. Expected cash flows are determined using expected payment information at the individual loan level, discounted using the effective interest rate. The effective interest rate generally ranges between 2 and 18 percent.

OREO that has been acquired or written down in the current year is deemed to be at fair value, which uses asset valuations. Asset values are determined using appraisals or other third-party value estimates of the subject property with discounts generally between 6 and 11 percent applied for estimated holding and selling costs and other external factors that may impact the marketability of the property. Changes to the value of the assets between scheduled valuation dates are monitored through continued communication with brokers and monthly reviews by the asset manager assigned to each asset. If there are any significant changes in the market or the subject property, valuations are adjusted or new appraisals ordered to ensure the reported values reflect the most current information.

Table of Contents

For financial assets and liabilities carried at fair value on a nonrecurring basis, the following table provides fair value information as of June 30, 2018 and December 31, 2017.

(Dollars in thousands)	June 30, 2018		
	Fair value measurements using:		
	Level 1 Level 2 Level 3		
	Fair value	inputs	inputs
Impaired loans	\$74,301	\$—	\$74,301
Other real estate remeasured during current year	21,105	—	21,105

	December 31, 2017		
	Fair value measurements using:		
	Level 1 Level 2 Level 3		
	Fair value	inputs	inputs
Impaired loans	\$72,539	\$—	\$72,539
Other real estate remeasured during current year	40,167	—	40,167

No financial liabilities were carried at fair value on a nonrecurring basis as of June 30, 2018 and December 31, 2017.

NOTE K - EMPLOYEE BENEFIT PLANS

BancShares sponsors noncontributory defined benefit pension plans for its qualifying employees (BancShares Plan) and former First Citizens Bancorporation, Inc. employees (Bancorporation Plan). The service cost component of net periodic benefit cost is included in salaries and wages while all other non-service cost components are included in other noninterest expense.

BancShares Plan

For the three and six months ended June 30, 2018 and 2017, the components of net periodic benefit cost are as follows:

(Dollars in thousands)	Three months ended June 30		Six months ended June 30	
	2018	2017	2018	2017
Service cost	\$3,362	\$2,934	\$6,791	\$6,310
Interest cost	7,131	7,069	14,188	14,449
Expected return on assets	(11,976)	(10,307)	(23,933)	(21,005)
Amortization of prior service cost	20	53	40	105
Amortization of net actuarial loss	3,548	2,193	6,794	4,427
Net periodic benefit cost	\$2,085	\$1,942	\$3,880	\$4,286

Bancorporation Plan

For the three and six months ended June 30, 2018 and 2017, the components of net periodic benefit cost are as follows:

(Dollars in thousands)	Three months ended June 30		Six months ended June 30	
	2018	2017	2018	2017
Service cost	\$624	\$670	\$1,286	\$1,341
Interest cost	1,592	1,682	3,179	3,365
Expected return on assets	(3,110)	(2,796)	(6,216)	(5,592)
Amortization of net actuarial loss	86	214	157	428

Net periodic benefit cost \$(808) \$(230) \$(1,594) \$(458)

No contributions were made during the three and six months ended June 30, 2018 to the BancShares or Bancorporation pension plans. We anticipate making a \$50.0 million contribution to the BancShares plan during 2018.

NOTE L - COMMITMENTS AND CONTINGENCIES

To meet the financing needs of its customers, BancShares and its subsidiaries have financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit, standby letters of credit and recourse obligations on mortgage loans sold. These instruments involve elements of credit, interest rate or liquidity risk.

Commitments to extend credit are legally binding agreements to lend to customers. Commitments generally have fixed expiration dates or other termination clauses and may require payment of fees. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future liquidity requirements. Established credit standards control the credit risk exposure associated with these commitments. In some cases, BancShares requires that collateral be pledged to secure the commitment, including cash deposits, securities and other assets.

Table of Contents

Standby letters of credit are commitments guaranteeing performance of a customer to a third party. Those commitments are primarily issued to support public and private borrowing arrangements, and the fair value of those commitments is not material. To mitigate its risk, BancShares' credit policies govern the issuance of standby letters of credit. The credit risk related to the issuance of these letters of credit is essentially the same as that involved in extending loans to clients and, therefore, these letters of credit are collateralized when necessary.

The following table presents the commitments to extend credit and unfunded commitments as of June 30, 2018 and December 31, 2017:

(Dollars in thousands)	June 30, 2018	December 31, 2017
Unused commitments to extend credit	\$10,119,455	\$9,629,365
Standby letters of credit	87,574	81,530
Unfunded commitments for investments in affordable housing projects	77,622	61,819

Affordable housing project investments were \$150.5 million and \$128.0 million as of June 30, 2018 and December 31, 2017, respectively, and are included in other assets on the Consolidated Balance Sheets.

Pursuant to standard representations and warranties relating to residential mortgage loan sales sold on a non-recourse basis, contingent obligations exist for various events that may occur following the loan sale. If underwriting or documentation deficiencies are discovered at any point in the life of the loan or if the loan fails to perform per the terms of the loan purchase agreement, typically within 180 days from the date of sale, the investor may require BancShares to repurchase the loan or to repay a portion of the sale proceeds. Other liabilities included reserves of \$830 thousand and \$882 thousand as of June 30, 2018 and December 31, 2017, respectively, for estimated losses arising from these standard representation and warranty provisions.

BancShares and various subsidiaries have been named as defendants in legal actions arising from their normal business activities in which damages in various amounts are claimed. BancShares is also exposed to litigation risk relating to the prior business activities of banks from which assets were acquired and liabilities assumed in the various merger transactions. Although the amount of any ultimate liability with respect to such matters cannot be determined, in the opinion of management, any such liability will not have a material effect on BancShares' consolidated financial statements.

NOTE M - ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME

Accumulated other comprehensive loss included the following as of June 30, 2018 and December 31, 2017:

	June 30, 2018		December 31, 2017	
(Dollars in thousands)	Accumulated other comprehensive loss	Deferred tax benefit	Accumulated other comprehensive loss, net of tax	Accumulated other comprehensive loss, net of tax
Unrealized losses on securities available for sale	\$(74,671)	\$(17,175)	\$(57,496)	\$(48,834)
Unrealized losses on securities available for sale transferred to held to maturity	(105,034)	(24,158)		